

TO: Files

CC: San Diego Audit Committee

FROM: Willkie Farr & Gallagher LLP

RE: Interview of Lincoln Ward on May 5, 2006

DATED: May 15, 2006

On Friday, May 5, 2006, Michael Schachter and Jesenia Ruiz de la Torre, in Willkie Farr & Gallagher LLP's capacity as counsel to the Audit Committee, interviewed Lincoln Ward. Also in attendance were Donielle Evans of KPMG. The interview took place in a conference room on the 3rd floor of the City Administration Building and lasted approximately two hours.

The following memorandum reflects my thoughts, impressions, and opinions regarding our meeting with Lincoln Ward, and constitutes protected attorney work product. It is not, nor is it intended to be, a substantially verbatim record of the interview.

Warnings

Mr. Schachter began the interview by explaining the circumstances and purpose of the City of San Diego's (the "City") creation of the Audit Committee, noting that information obtained during the course of the interview would be used, if relevant, in the Audit Committee's eventual report. Mr. Schachter explained that Willkie does not represent Mr. Ward and, thus, statements made during the interview are not covered by the attorney-client privilege. Nonetheless, we would be treating the information obtained during the interview as confidential, covered by the work-product privilege during the investigation, but any such privilege would likely be lost with the release of the Audit Committee's report. Mr. Schachter asked that Mr. Ward keep the interview confidential. Mr. Schachter further explained that, if requested, we would provide information from the interview to the SEC, the U.S. Attorney's Office or the City's outside auditor, KPMG, so it is important that Mr. Ward be accurate and truthful. Mr. Schachter emphasized that Mr. Ward should seek clarification of any question at any time.

Background

Mr. Schachter began the interview by asking Mr. Ward to describe his previous employment history. Mr. Ward stated that he is currently retired. Prior to retiring, he was the Vice President of Pacific Telephone Company for San Diego and Orange County (now AT&T). Mr. Ward served the City of San Diego as the head of the Zero Based Management Review (the "ZBMR") and as a member of the Blue Ribbon Committee (the "BRC").

Zero Based Management Review

Mr. Ward described his work as the head of the ZBMR, a group Mayor Golding created in the early 1990's to analyze the City's operations and recommend how the City could become more efficient. Mr. Ward developed an approach that the ZBMR utilized, by which a recently retired individual with expertise in senior management (an "Outside Consultant") would analyze various aspects of the City's operations. To implement this approach Mr. Ward would seek out qualified Outside Consultants and ask them to consider specific aspects of the City's operations which were related to their prior experience. After that analysis was completed, recommendations were developed by the Outside Consultant based on the various data that was analyzed, such as the relevant department's budgets and performance measurements, among other things. The recommendations generated by the Outside Consultant would be given to the head of the department that had been analyzed for his/her review and to ensure that the factual assumptions that were used by the Outside Consultant were accurate. After this review process was completed and the recommendations by the Outside Consultant were finalized, they were given to the City Manager. It was anticipated that the City Manager would, after reviewing the recommendations by the Outside Consultant, take measures to ensure that they were acted upon. A committee of the City Council was formed to follow up on the recommendations given to the City Manager to ensure they were put into effect. Mr. Ward noted that the recommendations became public documents 30 days after they were given to the City Manager. Mr. Ward stated that as a result of the work of the ZBMR, over a period of years that extended beyond his involvement with the BRC, the City saved approximately \$175 million.

As an example of the ZBMR's work, Mr. Ward described an analysis regarding the use of vehicles owned by the City. For that analysis, an Outside Consultant was retained who was a former senior manager at Hughes Aircraft. The consultant considered vehicle usage statistics and found that 25% of the vehicles in the City's fleet were rarely utilized. The consultant recommended to the City Manager that those vehicles be sold.

Mr. Schachter asked Mr. Ward whether he had any experience working with either Ed Ryan, the City Auditor and Comptroller, or Terri Webster, an Assistant Auditor. Mr. Ward recalled that Ryan had asked the ZBMR to review the operations of the City Auditor's Office which would include its organizational processes and auditing functions. Mr. Schachter asked Mr. Ward to discuss the findings of the ZBMR regarding the Auditor's Office. Mr. Ward recalled that his impression of the Auditor's Office was that the ledger and other systems used within that office were "horribly archaic." Mr. Ward also recalled that the Auditor's Office desperately needed to improve its computer systems, because too much was done manually. Mr. Ward also briefly discussed his impressions of Webster and Ryan. Mr. Ward stated that he met Webster after he joined the BRC, but that he knew Ryan prior to his appointment. In Mr. Ward's opinion, Ryan was an honest individual and Mr. Ward recalled that he preferred speaking with Ryan over Webster, because he respected Ryan more than Webster and he felt he could not count on information that Webster shared with him because it may have come from one of her superiors. Mr. Ward did not explain which of Webster's superiors could be giving her information aside from Ryan.

Blue Ribbon Committee

Mr. Schachter asked Mr. Ward why he was appointed to the BRC. Mr. Ward responded that he believed that he was appointed to the BRC because of his work on the ZBMR and his reputation as “a pretty good operations manager.” Aside from those reasons, Mr. Ward could not recall why he was appointed to the BRC. Mr. Schachter asked Mr. Ward what his relationship to the Mayor was prior to his appointment to the BRC. Mr. Ward stated that he did not know Mayor Murphy prior to his appointment to the BRC. While Mr. Ward did support Mayor Murphy with a small financial contribution of approximately \$50-\$100, he was not actively involved in the Mayor’s campaign and did not think that his appointment to the BRC was a result of his political affiliation. Mr. Ward could not recall who asked him to join the BRC, but he did not think that the Mayor personally contacted him.

After reviewing Exhibit 1, the May 7, 2001 BRC Minutes and Agenda, Mr. Schachter asked Mr. Ward whether the BRC had been established to consider the budget process, as the Minutes indicate. Mr. Ward recalled that the BRC was established to assess the financial health of the City. Mr. Schachter asked whether there was a particular issue that triggered the BRC’s establishment. Mr. Ward could not recall any specific problems, but stated there were a few issues “floating around” that needed to be considered, such as deferred maintenance (an issue related to the financial liabilities that accrued if City property was not properly maintained or was allowed to deteriorate). Mr. Ward recalled that Mayor Murphy spoke to the BRC and stated that he needed an independent assessment so that accurate recommendations could be made to improve the City’s financial condition.

Mr. Ward reviewed Exhibit 2, the June 15, 2001 BRC Minutes, which listed a number of issues which were addressed by the BRC, including the pension system. Mr. Schachter asked who brought the pension system to the BRC’s attention. Mr. Ward could not recall who suggested that the pension system be considered, but he thought that Richard Vortmann may have brought that issue to the BRC’s attention. Mr. Ward described Vortmann as a “champion of pension issues” who was very vocal about problems within the pension system. Vortmann had an inside perspective and was the major figure regarding pensions and unfunded liabilities. He also stated that Ryan and Webster supported Vortmann’s conclusions. Mr. Ward recalled that Vortmann is the President of NASCO and had some relationship with the SDCERS Board. Mr. Ward was shown Exhibit 3, an email from Webster to Vortmann, dated January 14, 2002, that stated that the biggest problem with the pension system was that the City was not fully funding its future liabilities. Mr. Schachter asked Mr. Ward what his opinions were regarding pension issues while he was a member of the BRC. Mr. Ward recalled agreeing with Vortmann regarding pension issues and Mr. Ward felt that the City not fully funding the system was a growing concern. Mr. Ward stated that he was not involved in the BRC’s analysis of pension issues.

Mr. Schachter asked Mr. Ward to describe the process the BRC engaged in during the preparation of its report. Mr. Ward stated that tasks were divided among BRC members so that there was a lead person on each issue and another member of the BRC who assisted the lead person. After an issue was explored, the lead person assigned to that topic would make a presentation to the BRC. Mr. Schachter asked Mr. Ward what topic he was assigned to and Mr. Ward responded that he took the lead role regarding deferred maintenance; Vortmann assisted

him. The issue of deferred maintenance dealt with how the deferral of maintenance projects affected the City's fiscal health. For example, while addressing the deferred maintenance issue, Mr. Ward considered the ways that not repairing the boiler or the door handles of a building could be a financial liability. Mr. Ward recalled that April Boling, of the BRC, was assigned to water and sewer issues. Mr. Ward could not recall learning about any issues regarding rate structures for the water or sewer department through his work with the ZBMR or the BRC.

Mr. Schachter asked Mr. Ward if he had ever seen Exhibit 4, the Blue Ribbon Committee Work Plan. Mr. Ward stated that he "sort of recognized it" and that it was probably developed by the Chairman of the BRC. Mr. Schachter asked Mr. Ward if the BRC had planned to complete its report by September 2001, as the Work Plan indicated. Mr. Ward recalled that being the BRC's goal. Mr. Ward reviewed Exhibit 5, the BRC Minutes of August 31, 2001, which indicated that he and Vortmann were giving a presentation to the BRC on that date. Mr. Ward acknowledged that at that point it appeared that the report was nearing completion, even though it was not released until February 2002. The reasons for that delay were then explored by Mr. Schachter. Mr. Ward was shown Exhibit 6, a handwritten note by Webster which stated "don't want to mess w/ ballpark bonds." Mr. Schachter asked Mr. Ward if he recalled any discussions regarding the Ballpark financing or the effect that the BRC's report could have on that financing. Mr. Ward recalled some general discussions with the BRC about the Ballpark financing, but he could not recall any conclusions on that topic. Mr. Ward did not think that any delays in the issuance of the BRC's report were "strategic." He thought that perhaps Joe Craver, Chairman of the BRC, could provide more details on this subject.

Mr. Ward was shown Exhibit 7, a letter authored by Vortmann, in which Vortmann wrote that "[t]he committee's unstated concern over the ballpark financing and any impact to the city's credit rating in general are now behind us." Mr. Schachter asked Mr. Ward what he thought that was referring to. Mr. Ward thought that Vortmann was stating the since the Ballpark financing was successful it was no longer at issue. Mr. Ward could not think of what else Vortmann may have been referring to. Mr. Ward reviewed Exhibit 8, an email that Vortmann sent him, dated January 3, 2002. Included in the email was a previous email written by Mr. Ward which stated that the BRC's report may have "a very deleterious impact on our bond ratings" Mr. Ward recalled that he did not think that this email referred specifically to the Ballpark financing, Mr. Ward thought that he was referring to bond ratings in general when he wrote that email. Mr. Ward recalled general discussions regarding the impact the BRC's report would have on rating agencies and there were discussions about the City's rating being positive. Mr. Ward could not recall who initiated those discussions, but it could have been Ryan, Webster, Boling, Vortmann, or Craven. It was Mr. Ward's understanding that if the bonds were impacted, the rating agencies would lower the City's ratings. Despite these conversations, Mr. Ward also recalled that ratings were not a concern; the primary concern was in issuing an accurate report. Mr. Schachter asked if the treatment of deferred maintenance could have an impact on the rating agencies' recommendations. Mr. Ward stated that it could have an impact as to costs, such as the costs of capital improvements. Mr. Schachter asked if Mr. Ward could recall any other reasons why the BRC's report may have been delayed. Mr. Ward responded that the report may have been delayed because there was a problem regarding the Mayor and the City Councilmembers' schedules. Mr. Ward recalled that there was a period when the BRC discontinued their work while Craven was finalizing the report. Mr. Schachter asked Mr. Ward if he thought that the events of September 11th impacted the issuance of the report. Mr. Ward stated that he did not

think that that was the reason for the delay. Mr. Ward reiterated that he did not think that any delays were strategic. Mr. Ward stated that it may have been someone's strategy to delay the BRC's report, but if so, "it was above his head."

Mr. Schachter asked Mr. Ward if he recalled any discussions regarding changing the tone of the BRC's report from negative to more positive. Mr. Ward stated that there were discussions among the BRC regarding the tone of the report. Mr. Ward reviewed Exhibit 9, an email from Webster, dated January 17, 2002. The email states "thank you for turning the tide on this issue." Mr. Schachter asked Mr. Ward what he thought Webster was referring to. Mr. Ward replied that he was not sure. Mr. Ward again reviewed Exhibit 8, an email that Vortmann sent him, dated January 3, 2002. Included in the email was a previous email written by Mr. Ward where he stated that "we may have inadvertently structured the potential for a media fest of 'accentuating the negative.'" Mr. Schachter asked him what he meant by that. Mr. Ward stated that he recalled thinking that some of the wording in the BRC's report might create a bigger red flag than was necessary. Mr. Ward recalled that Vortmann wanted to include what he viewed as strong language in the BRC's report with regards to pension issues. Mr. Ward recalled speaking, possibly to Ryan, regarding the language in the BRC's report being too inflammatory and how the language should be altered. Mr. Ward stated that he would need to review the previous language of the report to recall what language he may have been referring to. Moreover, Mr. Ward recalled thinking that while there were some areas of concern, there were some positive findings by the BRC and, based on his previous work on the ZBMR, he thought that San Diego was in a relatively good financial position. Therefore, he was sure that he influenced a more positive tone in the BRC's report, because he felt that that was factually accurate. Ultimately, Mr. Ward felt that the BRC issued a report that was accurate and more appropriate than previous drafts.

Mr. Schachter asked whether Mr. Ward thought that it was odd that the City delegated the task of responding to the BRC's report to SDCERS. Mr. Ward replied that he thought that it was, because the problems with the pension system had to do with unions influencing the City Council. Mr. Ward concluded that the City did not take any concerted action with regards to the BRC's recommendations. Mr. Ward stated that this was typical of Mayor Murphy who "did not act on much."

Mr. Ward reviewed Exhibit 10, an email he sent to Ryan and Webster, dated January 2, 2002, in which he asked them to let him "know privately" if they had any suggestions to his revisions. Mr. Schachter asked why Mr. Ward felt that he needed to discuss his revisions privately. Mr. Ward recalled that the email was regarding some fine tuning he had done on Boling's draft as a result of the interrelationship between deferred maintenance and water and sewer issues. Mr. Ward recalled wanting to get their opinions regarding a change in the wording of that section, but he could not recall any specifics beyond that.

Mr. Ward also reviewed Exhibit 11, the BRC Minutes of May 25, 2001, and it was noted that he was not in attendance at that meeting.

City Budgets

Mr. Schachter asked Mr. Ward if he had any experience with City budgets. Mr. Ward replied that outside of his involvement with the BRC, he observed that the City's budgets

were poorly done, that they were unrealistic, and that there should have been some long-term budgetary plans. Mr. Ward recalled that the budgets were poor, “sometimes even reckless.” Mr. Ward thought that it is important for the budgeting to be honest. As an example of the unrealistic nature of the budgeting process, Mr. Ward described how, within the police and fire departments, overtime pay was not properly calculated. Mr. Ward noted that the police department would ask for additional funds so that it could recruit officers, but if the new recruits were not hired, the police department would use those funds for whatever other purpose it deemed appropriate. Mr. Schachter asked Mr. Ward if the City used a “top-down” or a “bottom-up” budget. Mr. Ward explained that the City used a “top-down” budget.¹ Mr. Ward recalled that the budgets produced under City Manager Jack McGrory were a “farce.” City Manager Michael Uberuaga did not make any major improvements to the budget process, despite some efforts based on recommendations to implement a “bottom-up” budgeting strategy.² Recommendations were made for the City to engage in realistic long-term budgeting, rather than simply creating annual budgets, but the City was not successful in implementing that approach. Mr. Ward did not explain who made those recommendations or when the recommendations were made.

Remediation

Mr. Schachter asked Mr. Ward if he could suggest any methods of remediation. Mr. Ward stated that while working for the City he saw many things that would have resulted in someone being fired from a private company. Mr. Ward stated that he saw a great deal of evidence of poor management, but nothing he would classify as criminal conduct. Mr. Ward observed that pressure by the unions was a serious problem and he would recommend that the City Council, “who are beholden to the unions,” stand up against the unions. Mr. Ward also noted that there were people in the City who were out for personal gain, such as McGrory. Mr. Ward did not explain how McGrory was out for personal gain. Mr. Schachter then asked Mr. Ward if he could suggest any specific ways that the pension system could be improved, such as changing the composition of the Board. Mr. Ward stated that he could not think of any suggestions at that time.

Mr. Schachter concluded the interview by inviting further suggestions for remediation that Mr. Ward thought of at a later time, especially in light of his experience with City operations while working with the ZBMR.

WF&G

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¹ Note: A “top-down” budget is a budget where the first decision that is made is the size of the budget, then the composition of the budget is established.

² Note: When a “bottom-up” budget is used, various spending categories are decided on at one time and the total budget emerges at the end of the process by summing up the costs of the various spending programs.

EXHIBIT 1

Mayor Dick Murphy

**Blue Ribbon Committee
on
City Finances**

**Agenda
5/7/01**

- 1. Introductions**
- 2. Staff support role**
 - **Setting future meeting schedule**
 - **Attend meetings, provide minutes**
 - **Draft report**
- 3. Scope of activity**
- 4. FY 2002 Proposed Budget review schedule by Mayor and City Council**
- 5. Open Forum**

MAYOR DICK MURPHY
BLUE RIBBON COMMITTEE
ON
CITY FINANCES

Minutes of May 7, 2001 Meeting

*What was the
budget process?*

Mayor Murphy opened the first meeting with introductions and a proposed scope of activity (see attached). He indicated that the Committee goal would be recommendations to Mayor and Council in October and November 2001 for consideration on the budget process for fiscal year 2003. And that he convened the Committee now present to let them observe the current process and results.

The Mayor indicated that he had appointed Joe Craver as Chairman of the Committee.

Joe Craver initiated a discussion of the scope of work of the Committee and solicited input from the Committee members, particularly on how to address the first item on the Mayor's proposed scope of activity. - "What is a fair way to assess the general fiscal health of the City?"

The Chair scheduled the next meeting for Friday, May 11, 2001.

- B. How does the City of San Diego compare to other large cities in California and the United States on these criteria?
- C. Is the City adequately funding core services? Are adequate funds being spent on infrastructure and deferred maintenance?
- D. Is the City providing services that it should not be providing?

II. The following statements are the City's Six Budgeting Principles.

A. Are these Budgeting Principles sound?

1. Ongoing expenditures should be supported by ongoing revenues. Consequently, one-time revenues should not be used for ongoing expenditures on a continuous basis.
2. General Fund reserves should be maintained at approximately 3%.
3. When capital projects are considered, all associated costs should be identified in order to properly consider future financial impacts.
4. Each enterprise fund should reflect the true cost of operation, including direct and indirect costs of services provided by the General Fund.
5. Activities that are supported by user fees should be fully cost recoverable.
6. Discretionary General Fund revenues should not be earmarked, thereby allowing maximum flexibility in funding decisions on an annual basis.

B. Are the Budgeting Principles being followed?

Blue Ribbon Committee
Page 3
May 7, 2001

- C. Should the Budgeting Principles be changed?
- D. Should the Budgeting Process be changed?

III. Other Fiscal Issues

- A. Should the TOT tax be raised from the current 10.5%?
- B. Should the Transnet ½ cent sales tax for transportation projects be extended beyond 2008?
- C. Should the City support or oppose the Taxpayers Relief Act which requires a 2/3 vote on all tax increases (on the ballot in 2002)?

EXHIBIT 2

MAYOR DICK MURPHY
BLUE RIBBON COMMITTEE
ON
CITY FINANCES

Minutes of June 15, 2001 Meeting

April Boling, Vice-Chair of the Committee, opened the meeting at 1:00 p.m. Those attending were: Committee Members Andrew Poat, Dick Vortmann, Linc Ward, William McCurine, Victor Vilaplana, Mary Ball, Dennis Gibson, and staff Ed Ryan and Terri Webster.

At the prior two Committee meetings, there was agreement and direction to work towards a list of data and factors that would be used to evaluate the City's fiscal health. The committee began discussing the draft documents prepared by staff in response to this direction. The following information was presented, discussed, and some changes requested:

- Revenues per Capita
- Property Tax Revenue
- Expenditures per Capita
- Fund Balance

Information distributed but not discussed by Committee due to time was:

- Unfunded Pension Liability
- Pension Assets
- Fringe Benefits
- Comparative Credit Ratings of California and National Largest Cities

It was agreed that for the next two weeks staff will focus on preparing the fiscal factors requested for the General Fund only. At a future meeting the Committee will clarify for staff if any or all fiscal factors are needed for the Water, Sewer and CIP funds.

At the end of the meeting, there was discussion again on how to rate the fiscal health of the City. There was no change in direction to staff.

Linc Ward recommended scheduling out the future meetings and goals for each meeting to ensure timely completion of the committee's mission. He handed out a suggested outline as well as information on the mission statement.

Meeting adjourned at 2:40 p.m. The next meeting of the Committee will be Friday, June 22, 2001 at Cox Communications at 5159 Federal Blvd.

EXHIBIT 3

BRC

720535

General Inv Hot 3-21-06

Email message text
Object type: [GW.MESSAGE.MAIL]
Item Source: [Sent]
Message ID: [3C6B81FE.Demo-dom.Demo-PO.100.1676430.1.201F.1]
From: [Terri Webster]
To: []
Subject: [Re: Redraft of pension Sections]
Creation date: [1/14/2002 3:48:16 PM]
In Folder: [Mailbox]
Attachments: None
Message: [

Dick

Ed and I were talking about the BR report and something hit us. For the retirement section the biggest problem is that the City isn't fully funding it's future liability.....and it could be argued that the City does have a strategy to get back to paying 100% (it is just one strategy the committee does not like). But in the recommendations it does not say "City should fully fund". That is the point isn't it?

How about I suggest to April to modify in the executive summary and detail . Recommendation #2 " The Committee recommends the City change its funding strategy to result in the City fully funding its future obligations earned today which includes the pension benefits as well as health insurance " or however you want to say it.

April is trying to finalize the draft today so let me know your thoughts.
Terri

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720507

General Inv Hot 3-21-06

Email message text

Object type: [GW.MESSAGE.MAIL]

Item Source: [Sent]

Message ID: [3C6B81F2.Demo-dom.Demo-PO.100.1676430.1.200E.1]

From: [Terri Webster]

To: []

Subject: [Re: Draft Blue ribbon report 1/12/02]

Creation date: [1/14/2002 12:27:45 PM]

In Folder: [Mailbox]

Attachments: None

Message: [

April

Following are the rest of our comments . I will call you. Did you forward to Joe?

1. p. 4 #1 finding. Suggest adding after first sentence "This represents a substantial increase in reserves over the last 5 years". (this is supported by table on p. 11 which shows it more than doubled)

2. p. 5 Long term debt

a. Modify the last sentence "...which reflects a variety of very strong general credit characteristics such as the ability to repay long term debt, a diversified economy, moderate debt burden and strong financial management."

(.the ratings aren't just about the ability to repay debt...there is a variety of criteria considered)

b. take out "and" after Moody's

3. p. 5 Retirement (I'll contact Dick on this too). The problem should be quantified.

Suggest : Add as a second sentence " The City is not paying approximately \$6-8 a year for future pension benefits ."

Since the big problem is that under it's current strategy the City is not paying the full pension cost from the actuary.... somewhere in the recommendations it should say " The Committee recommends the City reconsider its present funding strategy and change to one that fully funds future pension costs earned today. "

4. p. 7 #6 R& E it needs to be clarified that the revenue numbers do not include carry over fund balance from the previous fiscal year. You can do it by a footnote to the number \$717 or modify the sentence to say"\$717 million, not including carry over fund balance." Without this it looks bad to see FY 02 Rev \$717 and expenses \$736 which look like we're headed for a deficit which is not accurate.

5. p. 10 chart: Footnote rec 1, 2, 6 with a comment that "the committee recognizes these recommendations are competing with each other for limited revenue dollars"....or something of that nature.

6. p. 37 A. 1. Again we recommend deleting the last two sentences. The committee should report on the current fiscal status and practice and not that which hasn't recently occurred. (I am finding more detail but for the last two budgets for FY 01 and FY 02 one time revenues were only used for one time expenses...I'm

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General Inv Hot 3-21-06

researching when the last time we did a land sale to "benefit" the general fund but it hasn't been in the last 2 years...at least ...so it shouldn't be in the report on current fiscal health)

7. p. 37 We get your distinction in #2 and would just make the last sentence "general funds reserve" and not General Fund reserves to clarify the issue.

We focused on the summary.... we'll give it an overall review again but this I think this version, with our suggested changes, it ready for the committee (EXCEPT FOR BOLINGS SECTION.....THAT IS HOLDING THE WHOLE PROCESS UP)

I'll call you.

Terri

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EXHIBIT 4

BLUE RIBBON WORK PLAN

May 11, 2001	Foundation meeting to review and agree on our objectives and work plan
May 25, 2001	Defined presentations and/or information we need for City staff
June 1, 2001	Strategic Plan presentation and discussion Assignment of task items
June 15, 2001	Criteria for evaluating the Fiscal Health of the City of San Diego
June 22, 2001	Planning presentation, discussion, recommendations Review "vision" draft (Review progress or cancel)
July 13, 2001	Key revenue sources and trends presentation Discussion of revenue recommendations Review "Planning" draft, assign tasks
July 20, 2001 27 1:00	Budgeting process presentation <ul style="list-style-type: none"> • Transparent/knowledgeable • Contingencies Discussion of budgeting recommendations Review revenue base draft (Review progress or cancel)
Aug 3, 2001	Sound cost management and performance evaluation Accounting and performance evaluation presentation Discussion of accounting and accountability recommendations Review budgeting process draft
Aug 17, 2001	Sound debt, cash management and related policies Debt policy, cash management presentation Discussion of debt/cash management recommendations Review "Cash Management and Performance Evaluation" draft
Sep 7, 2001	Final review of Task Force Report Present report to Mayor

Cancel 7/20
LINE OUTLINE

mayor 01/24/05
Report #2
EXHIBIT # 21

CAR00339

EXHIBIT 5

MAYOR DICK MURPHY
BLUE RIBBON COMMITTEE
ON
CITY FINANCES

Minutes of August 31, 2001 Meeting

Joe Craver, Chair of the Committee, opened the meeting at noon. Those attending were: Committee Members Joseph Craver, Andrew Poat, Dick Vortmann, Linc Ward, April Boling, William McCurine, and staff Ed Ryan and Terri Webster.

Linc Ward distributed the reports he and Dick Vortmann prepared on the City's ability to cope with the future needs of Water, Wastewater, Storm Drains and Multiple Species Conservation Program (MSCP). He gave a brief synopsis of their findings and conclusions.

Water and Wastewater are self funded programs which therefore have a limited impact on the City's overall financial health as long as the City stays with the programs' financing plans. In the case of Wastewater it is imperative to secure the Secondary Treatment EPA waiver renewal to avoid large fiscal impacts to the Wastewater Fund. Both Water and Wastewater have infrastructure needs that are being addressed thru their large financing programs.

Storm Drains has become a larger fiscal issue due to new State regulations issued to comply with the Federal Clean Water Act by 2006. The current revenue from storm drains fees is \$6million per year. It is estimated that costs could reach \$42 million per year to be in compliance with the new law. The City is developing a comprehensive plan for compliance which will include funding options for any shortfall between fee and costs. This new mandate presents a current funding issue for the City.

The MSCP is administered through a multi agency 1997 agreement which is estimated to cost \$50m a year for 20 years. The cost split between the agencies is not clear. Since the cost and funding split is not final, it is difficult to predict the exact impact to the City finances although it is estimated to be in the \$10-20m range. A strong effort to secure grants for this purpose is needed to minimize the cost to the City.

The Chair reminded everyone that he would be incorporating everyone's written report into the final document. He stated that each member would have a chance to make changes and suggestions that everyone would need to be comfortable with the final report.

Because of the amount of work needed to be done by the Chair, there will probably not be a meeting on Friday, September 7. The Chair requested everyone leave that meeting on their calendars until they hear from him.

The meeting was adjourned at 1:30 p.m.

EXHIBIT 6

BRC



858
292-5702
Art
Zarag
Bro
2/10/01

THE CITY OF SAN DIEGO
TERRA A. WEBSTER, C.P.A.
Assistant City Auditor and Comptroller
Office of the City Auditor and Comptroller
MS 6A • (619) 236-5566 • (619) 533-3998 (FAX) • email: ta@city.sanet.gov

MEMO

8-31-01
Brought up by committee
- timing & content of report
- don't want to mess w/ budget bonds

-
- line item for 8-27-01
- ZBML report
 - syracuse report w/ #2
 - citation award by CSMFO? emre
 - reason report
 -



VE SUM 03180

CONFIDENTIALITY REQUESTED UNDER LETTER OF MARCH 2, 2004

AUD-TWE-052-0320

PENSION_I.E0000058

EXHIBIT 7

BCC



NATIONAL STEEL AND SHIPBUILDING COMPANY
A GENERAL DYNAMICS COMPANY

RICHARD H. VORTMANN
PRESIDENT

April 29, 2002

Joseph Craver	Via Fax: 619/299-8955
Mary Ball	Via Fax: 619/265-5600
April Bbling	Via Fax: 619/667-7655
Dennis Gibson	Via Fax: 619/236-7228
Bill McCurine	Via Fax: 619/231-4765
Andrew Post	Via Fax: 619/234-2915
Aprilrose Riel	Via e-mail
Victor Vlaplana	Via Fax: 619/615-0310
Ed Ryan	Via Fax: 619/236-6219
Tern Webster	Via Fax: 619/236-6219
Linc Ward	Via Fax: 619/440-7050

Dear Fellow Blue Ribbon Committee Members:

With our committee now in "hibernation" until next Spring, as time has past and events gradually unfold at City Hall, I have been reflecting on our final report. As you might recall my redraft of Chairman Joe's initial draft was relative harsh in its appraisal of the City's fiscal health. After much discussion of whether the "sky was really falling" and did we really want to say all that, we, as a group, with my concurrence, evolved to the final version of our conclusion i.e. "the city is in good fiscal shape, but..."

Interestingly, the several "citizen comments" I have received regarding our report have all been essential the same - "yeah, my balance sheet and credit rating would be good too. If I didn't maintain my house and pay all my expenses."

The committee's unstated concern over the ball park financing and any impact to the city's credit rating in general are now behind us. However certain recent developments since our report deliberation seems to accentuate the "buts" we made in our report.

First the City's EPA waiver on the sewer plant is now in question, which, worst case, would result in an mandatory unplanned multi-billion dollar liability. Even if the waiver is finally granted it likely will come with new restrictions which will reduce the available capacity for population growth (and thereby invalidate our report's conclusion that the City had a viable plan for the future assuming the proposed rate increases were approved).

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Report #2
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NAV 00736
VE SUM 03171
Exhibit #37

Second, the City appears to be equivocating on approving the first (of several planned) user rate increases for the Water Department. Worse, regulators, apparently in frustration of lack of progress on improving water quality, are "threatening" to publicly question the safety of our water supply (which most likely would lead to significant mandatory increased spending in facilities).

Third, the issue of storm water containment appears to be heating up with a potential price tag far higher than the "unbudgeted" \$143m we stated in our report.

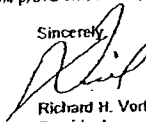
Fourth, as I continue to learn more about the City's pension system, coupled with the impact of the equity market bubble burst on the pension portfolio, it is clear the City has deferred to future taxpayers far more dollars than our report assumed. Further, there appears a chance the City will grant further pension benefits this year which will either increase the pension budget line item or (more likely) push yet more current costs out to future taxpayers. Unlike deferred maintenance, these are mandatory costs which ultimately must be paid, and these amounts explicitly grow with interest when they are deferred.

I have a growing and daunting concern that we possibly did our City a disservice by not ringing a very loud bell that:

- i) the City's fiscal health is not what it appears,
- ii) there are serious problems,
- iii) their solutions will be painful in terms of reduced services and/or increased taxes and fees, and
- iv) a comprehensive multi-year strategic plan to deal with the situation must immediately be developed; difficult decisions must be made now.

I offer these personal thoughts for the Blue Ribbon Committee's consideration. Even if you were all to share my concern on this issue, I am not certain of what to do next. I remain hopeful my fears expressed here will prove unfounded, but I am not optimistic.

Sincerely,



Richard H. Vortmann
President

RHV/h

VE SUM 03172

EXHIBIT 8

From: Dick Vortmann [dvortman@nassco.com]
 Sent: Thursday, January 03, 2002 10:44 AM
 To: Linc Ward
 Cc: April Boling; Terri Webster; Dvortmann1@aol.com; mary.ball@cox.com;
 jwcraver@galaxie.cnhost.com; ariel001@san.rr.com; vilaplana@scmv.com;
 WMcCurine@SWSSLAW.com; Andrew Poat
 Subject: Re: 12-30-01 draft

Linc

I basically agree with your position. It will not be my intent to "accentuate the negative". My objective is for the Committee to i) understand and agree on what is the true situation, and then ii) decide exactly how to describe it to the powers that be. The "sky is not falling" but on the other hand there are some, what appear to be, potentially serious issues that need to be comprehend in the City's five year strategic budget plan. How to get that done with out creating a publicity feeding frenzy or negatively impacting bond negotiations, etc. is the creative challenge.

Dick

Linc Ward wrote:

> Hi all: From Linc
 >
 > In the version which April Boling worked on so diligently and in which
 > she has incorporated some of Dick Vortmann's input I find that we have
 > inadvertently structured the potential for a media feast of "
 > accentuating the negative" and one which potentially might also have a
 > very deleterious impact on our bond ratings (we're telling them
 > they're wrong and should look deeper!)
 >
 > In no way do I intend in so saying to impugn or disparage either
 > April or Dick.
 > I just think we can cover the points (plus a few others) in a more
 > balanced fashion.
 >
 > In that context, what follows is a first cut of same:
 >
 > The Committee's general findings are:
 >
 > * The City is basically fiscally sound and by comparison with other major
 > cities is very well-managed. There is , however, room for improvement.
 >
 > * Revenue
 > As with some other California cities, San Diego operates within a
 > restricted
 > revenue base due to Propositions 13 and 218
 > The City's per capita revenues, thus, are lower than most major U. S.
 > Cities.
 > San Diego operates within the restrictions of the Peoples Ordinance-
 > adopted
 > in a different era- which precludes the collection of fees for
 > residential trash
 > collection.
 > San Diego does not utilize some revenue sources used by other
 > California cities to offset the restrictions of Proposition 13
 > (Utilities Users Tax and Documentary Transfer Tax).
 >
 > *Expense
 >

> San Diego , as with any government entity, has fiscal demands which
 > exceed current funding sources.

>

> While other cities have entered into debt to fund ongoing expenses,
 > San Diego has maintained an acceptable level of debt, and as a result
 > has retained a positive credit rating. Over the next few years the
 > City will incur major increases in debt.

> These

> increases are planned to be mitigated by revenue increases such that
 > debt service as a percentage of revenues is only increasing by 1
 > percentage point.

>

> The City in the last fiscal year reduced its reliance on one-time
 > revenues to fund on-going operations.

>

> Reserves

>

> The City has made progress in increasing the size of general fund reserves.
 > (in our detailed report the Committee recommends increasing this
 > effort)

>

> Areas of Concern

>

> *Operating within the restrictions identified above, decisions have
 > been made over the years to defer physical infrastructure requirements
 > in favor of more visible or other pressing needs While this situation
 > has been long in its creation and certainly not the product of current
 > City leaders, the incumbent Administration must publicly recognize the
 > need and develop plans to deal with it..

>

> *The City , likewise, has deferred the recognition of currently
 > incurred cost for pensions and retiree health care (ie: earned by
 > current employees to be collected in the future)

>

> *The City's principal Enterprise funds- Water and Wastewater- have
 > needs involving both deferred maintenance and infrastructure
 > investment. Plans have been developed to deal with these needs. These
 > plans call for significant and recurring user rate increases as well
 > as bond issues.

>

> *Current economic conditions (local and statewide) can have a
 > material impact on City revenue in the near term

>

> In sum, the Committee feels it is incumbent on the City to develop a
 > long range financial and operations plan to address these issues and
 > to fully apprise the public of the issues and of the plans,

>

> The Committee believes San Diego has earned the self-proclaimed title
 > of America's Finest City and that the City is poised to perpetuate
 > that title. How well the City deals with the issues raised in this
 > report will play heavily in how deserved that title will be in the
 > future as well as the Mayor's goal as a "City worthy of our
 > affection."!

EXHIBIT 9

Mail

[Previous](#)

[Next](#)

From: Terri Webster
To: "mar-lin@pacbell.net".SMTP Gateway.LANLAB
CC: Ryan, Ed
Date: 1/17/2002 1:34 PM
Subject: Report

Linc

Thanks for the offer to front any issues.... we are happy with the report as worded so at this point just looking forward to hopefully an unanimous approval. Dick V. already gave his thumbs up so that's a big hurdle. Thank you for "turning the tide" on this issue !
Terri

EXHIBIT 10

720177

General Investigation Hot 3-17-06

From: Linc Ward

It: Wednesday, January 02, 2002 1:48:45 PM

To: Ed Ryan; Terri Webster

Subject:

Hope u got the "revision " I suggested top April's version.
Let me know privately if u have any suggestions vs what I wrote.

Linc

EXHIBIT 11

MAYOR DICK MURPHY
BLUE RIBBON COMMITTEE
ON
CITY FINANCES

Minutes of May 25, 2001 Meeting

Joe Craver, Chair of the Committee, opened the meeting at Noon. Those attending were: Committee Members Joseph Craver, Andrew Poat, Dick Vortmann, April Boling, April Rose Riel, and staff Ed Ryan and Terri Webster.

The Chairman said that it was imperative that this committee decide quickly on the Mission Statement and Goals. Once that is decided, we can bring closure to what we have been asked to do. There is an end to our task. We need to complete our tasks within five to six months max.

At the Chair's request, Dick Vortmann gave a brief synopsis of the special budget meeting that was held on May 21 for the benefit of those that were unable to attend.

The Chair then presented a Mission Statement that is a compilation of suggestions from committee members:

MISSION STATEMENT

Perform an independent evaluation of the fiscal health of the City of San Diego.

To review the budgeting principles of the City of San Diego.

Report the findings and recommendations to the City Rules Committee.

A discussion followed among the members with April Boling stating she felt that some things that the Mayor requested were being cut by this Mission Statement. After further discussion, it was agreed that this Mission Statement allowed the committee to go forward with their tasks without being overly explicit. The Chair reminded the committee that the members present make the decisions and the issue wouldn't be revisited at a later date. The members agreed and there was a resolution in support of the Chair's approach.

Terri Webster presented a list of City Charter mandated functions. April Boling stated that she felt the task of deciding what is core versus non-core functions should be reserved for the elected officials. Dick Vortmann felt that we should take a current assessment of the City's fiscal health by using a balance sheet approach. April Rose Riel felt that we need a more global perspective. Andrew Poat felt we do not have the time or resources to do a performance evaluation of the City. Joe Craver felt the key question is "How fiscally sound is the City—good, bad, or poor? What the City is doing—is it good, bad or poor? The Mayor wants to know from an independent source (this committee) if the City is fiscally sound. In order to answer that question this committee needs to be smart. Keep our task simple but very effective."

The Chair asked Ed Ryan's opinion on how to proceed. He suggested that the Committee start by identifying what factors they need to assess the health of the City. He suggested:

- Ryan did not know person that come up.
- A. Revenues per Capita
Analysis of revenues to the population over five years. If revenues are decreasing, the City may be unable to maintain existing service levels unless it finds new sources of revenues or ways to save money. Also compare to other cities.
 - B. Expenditures Per Capita
Analysis of expenditures to population. If the trend is increasing over the years, it may indicate that the cost of providing services is outstripping the community's ability to pay. Also compare to other cities.
 - C. Funds Balance
Analysis of unreserved fund balance to revenues. The size of the City's fund balances can affect its ability to withstand financial emergencies and accumulate funds for capital purchases without having to borrow. A decline in fund balance may mean the City may be unable to meet future needs.
 - D. Debt Service
Analysis of net direct debt service versus net operating revenues. Debt service is the amount of principle and interest that the City must pay each year on net direct bonded long-term debt plus interest on short term debt. Debt service can be a major part of the government's fixed costs, and increases may indicate excessive debt and financial strain.
 - E. Credit Rating by Major Rating Agencies
As the major rating agencies review the City frequently, it makes sense to use their analysis.
 - F. Condition of Assets
 - Deferred Maintenance
 - Streets
 - Buildings
 - Information Technology
 - Fleet
 - Retirement
 - Water
 - Sewer
 - Storm Water

to begin with and that the Committee could add others should they feel the need as the work progressed. They agreed.

The Chair suggested that Ed arrange for someone from the City Manager's office present a 2001 budget review. He asked April Boling, Vice Chair, to work with Ed and April Riel to schedule that meeting. The Chair will be on vacation until June 18 and asked that the Committee continue the work without him.